



## INDONESIA: ECONOMIC AND FINANCIAL HIGHLIGHTS JUNE 2005

### Summary:

- Year-on-year (YoY) consumer price inflation remained at the 7.4 percent level in June 2005 and the rupiah weakened by 3.2 percent against the U.S. dollar.
- Bank Indonesia (BI) raised short-term interest rates by 23 basis points during the month in an effort to reduce money market liquidity and dampen inflationary pressures.
- On June 30, BI announced "anchor bank" criteria under the bank consolidation component of its "Indonesian Banking Architecture" plan.
- BI also issued important new regulations on risk management for mutual funds, foreign exchange transactions, and minimum capital requirements for banks operating under Islamic law.
- The Government of Indonesia (GOI) issued 15-year bonds for the first time on June 15.
- Indonesia's second largest telecommunications company, PT Indosat, issued USD 250 million of seven-year bonds in New York on June 15.
- State-owned power company PLN announced plans for a tariff increase in 2006 and also requested an increased subsidy from the Ministry of Energy and Mineral Resources.
- Rating agency Moody's raised its ratings for Indonesia's fifth and seventh largest domestic banks, Bank Danamon Indonesia and Bank Permata, and BI approved a merger between Bank Artha Graha and publicly listed Bank Inter-Pacific.

### CPI Inflation Remains Unchanged

The Central Bureau of Statistics (BPS) reported on July 1 that YoY consumer price inflation (CPI) in June 2005 was 7.4%, the same level as the month before. Month-on-month (MoM) CPI inflation was 0.50%, and January-June 2005 CPI inflation reached 4.28%. All CPI expenditure groups showed price increases from the previous month.

CPI Inflation Components (June 2005)	MoM	YoY
Foodstuff	0.73	5.30
Prepared food, beverages, cigarette and tobacco	1.17	7.82
Housing, water, electric, gas and fuel	0.25	6.88
Clothing	0.40	4.90
Health	0.32	3.88
Education, recreation and sport	0.16	10.48
Transport, communication and financial services	0.24	12.50
<b>Total</b>	<b>0.50</b>	<b>7.42</b>

Source: Central Bureau of Statistics (BPS)

BI has taken a number of recent steps to control inflation and bolster the rupiah, which has depreciated by 4.3% against the U.S. dollar so far in 2005. These include raising short-term interest rates (SBI rate) by 83 basis points since January 2005, reactivating an overnight to two weeks deposit facility (FASBI) for banks, and increasing the maximum allowed interest rate for rupiah and dollar deposits covered by the GOI's blanket guarantee. BI and the GOI also announced on July 5 that they would require state-owned enterprises to deposit their dollars in Indonesian banks, and have reportedly made arrangements for state oil company Pertamina to acquire dollars directly from BI's foreign exchange reserves (instead of purchasing dollars on the spot market). Pertamina requires large amounts of dollars to purchase refined oil products.

### **Bank Indonesia Announces “Anchor Bank” Criteria**

On June 30, BI announced “anchor bank” criteria under its 2005-2010 bank consolidation plan. BI hopes that medium and large anchor banks will have the capacity to expand their market share without compromising prudential banking principles. All banks must meet a set of minimum performance criteria by 2010, with those meeting additional requirements to be designated as anchor banks. BI stated “many banks have the potential to become anchor banks, though we would prefer to see as few as possible.” Criteria for anchor banks include:

- Strong and stable capital: minimum capital adequacy ratio (CAR) of 12% and minimum Tier 1 capital ratio of 6%.
- Sound profitability: minimum return on asset (ROA) of 1.5%.
- Healthy intermediary function as reflected in prudent loan expansion: minimum loan growth of 22% per annum or a minimum loan-to-deposit ratio (LDR) of 50% and a net non-performing loan (NPL) ratio below 5%.
- Anchor banks should be, or plan to become, limited liability companies under Indonesian law.
- Anchor banks should have met the criteria required for “well-performing banks” for the last three years, including: (1) core capital above Rp 100 billion (USD 10.2 million); (2) minimum CAR of 10%; (3) good ratings on corporate governance and sound management.

BI will encourage banks to restructure that fail to qualify as anchor banks because they have insufficient capital, are financially weak, have limited market share, or lack competitiveness. BI will give these banks three options: acquisition by an anchor bank, merger with one or more non-anchor banks, or a combination merger of a number of non-anchor banks with an anchor bank. BI will seek to identify similarities in operations, market segment, ownership links, and business orientation between non-anchor banks. There are currently 133 banks in Indonesia, 52 of which have less than Rp 100 billion (USD 10.2 million) in capital.

### **BI Issues New Prudential Regulations**

In response to the increasing number of banks marketing mutual funds, on June 14 BI issued circular letter No. 7/19/DPNP on the implementation of risk management in banks managing mutual funds. The circular outlines procedures to strengthen risk management practices in banks managing mutual funds.

Also on June 14, BI issued a new regulation, No. 7/14/PBI/2005, tightening controls on rupiah transactions and foreign currency lending by banks in order to prevent speculation against the rupiah. The new rules limit foreign exchange derivative transactions with foreign counterparts to USD 1 million, a reduction from the previous limit of USD 3 million. Previously unlimited dollar purchases in simple forward and swap transactions are also limited to USD 1 million. Derivative transactions conducted for hedging purposes are allowed but must be maintained for a minimum duration of three months. These restrictions do not apply to financial transactions when there is an underlying real sector transaction, such as trade or foreign direct investment.

Effective June 10, BI issued regulation No. 7/13/PBI/2005 setting the minimum capital adequacy ratio (CAR) for syariah banks at 8% of risk-weighted assets.

### **Government Sells Its First 15-Year Bonds**

On June 14, the government sold its first-ever 15-year bonds, raising more than Rp. 1 trillion (USD 102 million). Rahmat Waluyanto, a senior official at Directorate General for the State Treasury in the Ministry of Finance (MOF), told the media that the cost of issuing long-term debt was attractive because of the small spread between long-term and short-term yields. The MOF auctioned the 15-year bonds at a yield of 11.59%. It also sold Rp. 2.8 trillion (USD 285.6 million) in 11-year bonds at an average yield of 11.25%. The latest auctions mean the MOF has raised about Rp. 29.9 trillion (USD 3 billion) from debt issues so far this year, about 70% of its 2005 target. Before the MOF issued the 15-year bonds, the longest tenor GOI debt was 12-year bonds.

### **Surabaya Stock Exchange Launches Fixed Income Trading System**

On June 16, the Surabaya Stock Exchange (SSX) launched its Fixed Income Trading System (FITS) for scripless corporate bonds. By offering securities in small denominations (Rp 10-50 million, or USD 1,000–5,000), SSX hopes FITS will increase the number of retail investors in the corporate bond market. In its first transaction day, FITS recorded a transaction value of Rp. 1.9 billion (USD 0.2 million). Investors may still trade corporate bonds over the counter.

### **Telco Company Issues Bonds**

On June 15, Indonesia's second largest telecommunications company, PT Indosat, sold USD 250 million of seven-year bonds in New York. The bonds pay a 7.125%

coupon and will mature in 2012, to yield 7.250%. Indosat officials cancelled the New York leg of a roadshow promoting the bond issuance because of strong demand from investors. According to Dow Jones, Asian investors bought 45% of the issue, European investors 31%, and U.S. investors 24%.

### **PLN Calls for Increased Subsidy**

State-owned power company PLN announced a plan to increase electricity tariffs by 12.5% in 2006 during a June 6 hearing by Parliament's Commission VII. According to internal financial reports, PLN's operating costs have jumped by Rp 14 trillion (USD 1.4 billion) in 2005 due to March 1 fuel price hikes (PLN generates approximately 30% of its power using diesel generators). PLN hopes to save Rp 1.3–1.8 trillion (USD 133–184 million) by increasing its efficiency, but will ask the GOI to increase its subsidy by Rp 12.7 trillion (USD 1.3 billion) to cover the rest of the cost. PLN President Director Eddie Widiono said that PLN has already submitted a proposal to raise its subsidy to the Minister of Energy and Natural Resources.

### **Moody's Ups Domestic Banks' Rating**

Moody's Investors Service raised its financial strength ratings for two Indonesian banks in June. On June 6 Moody's raised the financial strength rating for Indonesia's seventh largest bank, Bank Permata, from E to E plus with a positive outlook. On June 28, Moody's announced that it had raised its rating for Indonesia's fifth largest bank, Bank Danamon, from E plus to D minus.

Permata, which has a 3% share of system deposits, was formed in September 2002 from an amalgamation of five banks taken over by the Indonesian Bank Restructuring Agency during the financial crisis. In October 2004, a consortium of Standard Chartered Bank and Indonesian car manufacturer Astra International acquired 51% of Permata from IBRA's successor, the state-owned Asset Management Company (PPA), which still holds 26.17% of Permata. As of April 2005, the consortium had upped its stake to 63.11%. The consortium aims to align Permata with Standard Chartered's standards, especially in risk management.

Danamon has a 5% share of the deposit market, with assets of Rp. 60 trillion (USD 6.1 billion) as of March 2005. A consortium of the Singaporean Government-owned Temasek Holdings (85%) and Deutsche Bank (15%) holds a 65.76% stake in the bank. To expand its business, which centers on consumers and small and medium enterprises, Danamon acquired a 75% stake in Adira Finance for Rp 850 billion (USD 86.7 million) in April 2004. Adira specializes in auto and motorcycle financing, and holds a 12-% market share in the motorcycle financing business.

### **BI Approves Bank Merger**

On June 15, BI approved the merger of Bank Artha Graha, a mid-sized commercial domestic bank (with links to the Indonesian military) with publicly listed

Bank Inter-Pacific. In its authorization letter, BI said the objective of the merger was to strengthen the banks' capital structure in line with BI's "Indonesian Banking Architecture."

Merged Banks' Financial Indicators (as of March 2005)	Artha Graha	Inter-Pacific
Assets <sup>(1)</sup>	8.3	0.3
Equity	0.6	0.1
Loans	5.5	0.1
CAR <sup>(2)</sup>	11.4	153.0

Source: Bank Indonesia

(1) Assets, equity, and loans in Rp trillion

(2) Capital Adequacy Ratio, in %

### Selected Economic, Monetary & Financial Statistics

	Mar 05	Apr 05	May 05	Jun 05
CPI Inflation (YoY)	8.81	8.12	7.40	7.42
CPI Inflation (MoM)	1.91	0.34	0.21	0.50
Rp/USD Exchange rate <sup>1</sup>	9,510	9,570	9,480	9,713
30-day SBI Interest Rate <sup>2</sup>	7.44	7.70	7.90	8.25
Foreign reserves <sup>3</sup>	36.03	37.32	34.61	34.38
JSX Composite Index	1080.2	1029.6	1088.2	
JSX Trans Volume <sup>4</sup>	2,984	1,405	1,339	
Exports (USD billion)	7.25	6.79	7.21	
% Change (YoY)	42.95	31.12	30.79	
Import (USD billion)	4.98	5.02	4.96	
% Change (YoY)	59.11	33.85	37.18	
Trade Balance <sup>5</sup>	2.27	1.73	2.25	

Source: Bank Indonesia, BPS

(1) Rp/USD, end of period

(2) End of period

(3) USD billions, end of period

(4) Jakarta Stock Exchange average daily transaction volume, in billions of shares

(5) USD billions

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